

**BLACK HILLS EDUCATIONAL  
BENEFITS COOPERATIVE**

**FINANCIAL STATEMENTS**

**JUNE 30, 2014 AND 2013**



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
JUNE 30, 2014 AND 2013

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
Black Hills Educational Benefits Cooperative  
Sturgis, South Dakota

### Report on the Financial Statements

We have audited the accompanying financial statements of Black Hills Educational Benefits Cooperative, (the Cooperative) (a public entity risk pool) as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Cooperative's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether



## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

### **Opinions**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Black Hills Educational Benefits Cooperative, as of June 30, 2014 and 2013, and the respective changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### **Other Matters**

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 7 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.





## INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

Management has omitted certain revenue and claims development information that governmental accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated November 12, 2014 on our consideration of the Cooperative's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Cooperative's internal control over financial reporting and compliance.

*David Pummel & Associates, LLP*

Belle Fourche, South Dakota  
November 12, 2014





INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING  
STANDARDS*

To the Board of Directors  
Black Hills Educational Benefits Cooperative  
Sturgis, South Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Black Hills Educational Benefits Cooperative, (the Cooperative) (a public entity risk pool) as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which comprise the basic financial statements, and have issued our report thereon dated November 12, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Cooperative's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a



INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING  
STANDARDS* (CONTINUED)

deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a certain deficiency in internal control described in the accompanying schedule of findings and questioned costs as item 2014-1 that we consider to be a significant deficiency.

#### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Cooperative's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings as item 2014-2.

#### **Cooperative's Response to Findings**

The Cooperative's written response to the findings identified in our audit is described in the accompanying schedule of findings. We did not audit this response and, accordingly, we express no opinion on it.





INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING  
STANDARDS (CONCLUDED)

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, as required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

*David Pummel & Associates, LLP*

Belle Fourche, South Dakota  
November 12, 2014



**BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**JUNE 30, 2014**

This section of Black Hills Educational Benefits Cooperative's (BHEBC) annual financial report presents discussion and analysis of BHEBC's financial performance during the fiscal year ended on June 30, 2014. Please read it in conjunction with BHEBC's financial statements, which follow this section.

**FINANCIAL HIGHLIGHTS**

- BHEBC's net position decreased \$62,932; cash increased 394.2%, while investments decreased 24.28%.
- During the year, BHEBC's revenues generated from premiums and investment income were \$62,932 less than the \$4,175,912 in expenditures.
- The total cost of BHEBC's programs decreased by 24.85% which was primarily due to a significant decrease in net claims paid. Professional fees increased because the actuarial study was not required for all districts this year.
- The proprietary fund reported a \$62,932 current year deficit due to lower than anticipated premiums and in investment income.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This annual report consists of two parts - management's discussion and analysis (this section) and the basic financial statements.

Proprietary fund statements offer short and long-term financial information about the activities that BHEBC operates like a business.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

**Fund Financial Statements**

The fund financial statements provide more detailed information about BHEBC's one fund. Funds are accounting devices used to keep track of specific sources of funding and spending for particular purposes. Fund accounting is required by South Dakota State Law.

BHEBC's operations fall under the Proprietary Fund type.

Proprietary Fund - Services for which BHEBC charges a fee are reported in a proprietary fund. The insurance fund is the only fund maintained by BHEBC.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)  
JUNE 30, 2014

FINANCIAL ANALYSIS OF BHEBC AS A WHOLE

Net Position

BHEBC's combined statement of net position increased as follows:

Table A-1  
Black Hills Educational Benefits Cooperative  
Statement of Net Position

	Proprietary Fund Activities FY 2014	Proprietary Fund Activities FY 2013
Current Assets	\$ 3,032,582	\$ 3,561,939
<b>Total Assets</b>	<u>\$ 3,032,582</u>	<u>\$ 3,561,939</u>
Current Liabilities	\$ 396,819	\$ 863,244
<b>Total Liabilities</b>	<u>\$ 396,819</u>	<u>\$ 863,244</u>
Unrestricted Net Position	\$ 2,635,763	\$ 2,698,695
<b>Total Net Position</b>	<u>\$ 2,635,763</u>	<u>\$ 2,698,695</u>
Beginning Net Position	\$ 2,698,695	\$ 4,266,506
Change in Net Position	( <u>\$ 62,932</u> )	( <u>\$ 1,567,811</u> )
 <b>Percentage of Decrease in Net Position</b>	 ( 2.33%)	 ( 36.75%)

The Statement of Net Position reports all financial and capital resources. The Statement presents the assets and liabilities in order of relative liquidity. The liabilities of BHEBC, consisting of fees payable and claims incurred but not paid, have been reported in this same manner on the Statement of Net Assets. The difference between BHEBC's assets and liabilities is its net position.

**Changes in Net Assets**

BHEBC's revenues totaled \$4,112,980. (See Table A-2.) Most of BHEBC's revenue comes from Other Revenue - Local Sources i.e. premiums from member districts. BHEBC's expenses cover support services, which include board services, fiscal services; and non-programmed charges, which include insurance premiums, claims, claims services.





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)  
JUNE 30, 2014

**BUSINESS-TYPE ACTIVITIES**

Table A-2 also considers the operations of the business-type activities.

Revenues from BHEBC's business-type activities increased by 3.11% to \$4,112,980 and expenses decreased by 24.85% to \$4,175,912. Factors contributing to these changes include:

- Revenues increased because of an increase in investment income and an increase in premiums from the prior year.
- The primary reason for the decrease in expenses is a 31.75% decrease in the net claims paid, which was offset by an 18.83% increase in premiums paid, a 53.3 % increase in administration fees, as well as an increase in professional fees (actuarial study was not required for any of the districts).
- The increase in premium income correlated to the increase in premiums and fees paid. Enrollment remains relatively stable.

**Table A-2**  
**Black Hills Educational Benefits Cooperative**  
**Changes in Net Position**

	<b>Total Proprietary Fund Activities FY 2014</b>	<b>Total Proprietary Fund Activities FY 2013</b>
<b>Revenues</b>		
Earnings from		
Investments & Deposits	\$ 36,684	(\$ 10,669)
Other Revenue - Local		
Sources	4,076,296	3,999,608
<b>Total Revenues</b>	<u>4,112,980</u>	<u>3,988,939</u>
<b>Expenses</b>		
Support Services	24,831	75,865
Non-Programmed Charges	4,151,081	5,480,885
<b>Total Expenses</b>	<u>4,175,912</u>	<u>5,556,750</u>
<b>Decrease in Net Position</b>	( <u>\$ 62,932</u> )	( <u>\$ 1,567,811</u> )
<b>Ending Net Position</b>	<u>\$ 2,635,763</u>	<u>\$ 2,698,695</u>



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
MANAGEMENT DISCUSSION AND ANALYSIS (CONCLUDED)  
JUNE 30, 2014

**FINANCIAL ANALYSIS OF BHEBC'S FUND**

The Proprietary Funds decreased \$62,932 this year. Future premium and claim increases will be covered by increased premium rates and reserves.

**BUDGETARY HIGHLIGHTS**

The Board approves a preliminary budget in May and adopts the final budget in August.

**CAPITAL ASSET ADMINISTRATION**

BHEBC has not acquired any capital assets.

**LONG-TERM DEBT**

BHEBC has not and cannot incur any long-term debt.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

BHEBC's current economic position has seen another decrease in fund balance. This decrease can be attributed to the practice of increasing premiums by less than the industry standard. Premium increases will exceed the traditional 5 percent resulting in a loss of grandfather status under the Affordable Care Act. The overall budget for next year increased significantly to correspond to increase in premiums and projected claims.

**CONTACTING BHEBC'S FINANCIAL MANAGEMENT**

This financial report is designed to provide citizens, taxpayers, customers, investors and creditors with a general overview of BHEBC's finances and to demonstrate BHEBC's accountability for the money it receives. If you have questions about this report or need additional information, contact Black Hills Special Services Cooperative's Business Office, P.O. Box 218, Sturgis, SD 57785.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
STATEMENTS OF NET POSITION  
JUNE 30, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
<b>CURRENT ASSETS</b>		
Cash	\$ 564,913	\$ 114,307
Accounts receivable	60,008	269,248
Prepaid insurance	1,476	689
Investments	<u>2,406,185</u>	<u>3,177,695</u>
<b>TOTAL CURRENT ASSETS</b>	<u>\$ 3,032,582</u>	<u>\$ 3,561,939</u>
 <b>CURRENT LIABILITIES</b>		
Unearned revenue	\$ --	\$ 130,767
Fees payable	62,693	--
Claims incurred but not reported	<u>334,126</u>	<u>732,477</u>
<b>TOTAL CURRENT LIABILITIES</b>	<u>396,819</u>	<u>863,244</u>
 <b>NET POSITION - UNRESTRICTED</b>	<u>2,635,763</u>	<u>2,698,695</u>
 <b>TOTAL CURRENT LIABILITIES AND NET POSITION</b>	<u>\$ 3,032,582</u>	<u>\$ 3,561,939</u>

See accompanying notes.





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
STATEMENTS OF REVENUE, EXPENSES, AND CHANGES IN NET POSITION  
FOR THE YEARS ENDED JUNE 30, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
<b>OPERATING REVENUE</b>		
Premiums	\$ 4,076,296	\$ 3,999,608
<b>OPERATING EXPENSE</b>		
Advertising	481	565
Administration	191,119	124,670
Claims	3,350,034	4,908,514
Directors' fees	2,850	3,225
Insurance premiums	604,528	509,376
Professional fees	26,900	10,350
Office expense	--	50
	<u>4,175,912</u>	<u>5,556,750</u>
<b>OPERATING LOSS</b>	( 99,616)	( 1,557,142)
<b>NONOPERATING REVENUE (EXPENSE)</b>		
Investment income	90,537	147,037
Net realized gain (loss) on investments	( 38,109)	8,034
Net unrealized gain (loss) on investments	( 15,744)	( 165,740)
	<u>36,684</u>	<u>( 10,669)</u>
<b>DECREASE IN NET POSITION</b>	( 62,932)	( 1,567,811)
<b>NET POSITION - BEGINNING OF YEAR</b>	<u>2,698,695</u>	<u>4,266,506</u>
<b>NET POSITION - END OF YEAR</b>	<u>\$ 2,635,763</u>	<u>\$ 2,698,695</u>

See accompanying notes.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash receipts from participants	\$ 3,939,159	\$ 4,130,375
Claims paid	( 3,532,775)	( 4,844,687)
Cash payments for insurance	( 605,315)	( 509,024)
Cash payments for administration	( 128,426)	( 124,670)
Other operating cash payments	( 30,231)	( 14,190)
<b>NET CASH USED IN OPERATING ACTIVITIES</b>	( <u>357,588</u> )	( <u>1,362,196</u> )
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sale of investments	717,657	2,112,283
Purchase of investments	--	( 1,000,225)
Investment income	<u>90,537</u>	<u>147,037</u>
<b>NET CASH PROVIDED BY INVESTING ACTIVITIES</b>	<u>808,194</u>	<u>1,259,095</u>
<b>NET INCREASE (DECREASE) IN CASH</b>	450,606	( 103,101)
<b>CASH - BEGINNING OF YEAR</b>	<u>114,307</u>	<u>217,408</u>
<b>CASH - END OF YEAR</b>	<u>\$ 564,913</u>	<u>\$ 114,307</u>
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating loss	(\$ 99,616)	(\$ 1,557,142)
Adjustments to reconcile operating loss to net cash provided by operating activities		
Decrease (increase) in		
Accounts receivable	209,240	( 105,046)
Prepaid insurance	( 787)	352
Increase (decrease) in		
Deferred revenue	( 130,767)	130,767
Claims payable	( 398,351)	168,873
Fees payable	<u>62,693</u>	<u>--</u>
<b>NET CASH USED IN OPERATING ACTIVITIES</b>	( <u>\$ 357,588</u> )	( <u>\$ 1,362,196</u> )

See accompanying notes.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014 AND 2013

**NOTE 1 - DESCRIPTION OF THE COOPERATIVE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Description of the Cooperative

The Black Hills Educational Benefits Cooperative (the Cooperative) is a public entity risk pool organized as a cooperative education service unit, comprised of member public entities. The Cooperative was organized July 1, 1996 to provide employee health benefit services to employees of member public entities through a partially self-funded plan. Risk is assumed by Black Hills Educational Benefits Cooperative. Member public entities are not liable for claims in excess of Cooperative assets. The goal of the Cooperative is to assist participating member public entities in providing appropriate benefits for all employees and families on a cooperative basis, services that these public entities would not be able to provide as effectively or as economically acting alone. Public entities seeking membership must be approved by an affirmative vote of a majority of the members of the Board of Directors. Any member entity may withdraw from the Cooperative by action of its Board of Directors. Withdrawal notice shall be made prior to February 1 for the succeeding school year. The Board of Directors can raise premiums or commit participating entities to obligations beyond the membership period. The Cooperative cannot enter into any long-term debt. A third party administrator is selected to administer all claims and secure reinsurance and other insurance coverage. Plan members currently are Black Hills Special Services Cooperative, New Underwood School District 51-3, Wall School District 51-5, Custer School District 16-1, Oelrichs School District 23-3, and Belle Fourche School District 9-1.

Summary of Significant Accounting Policies

1. Basis of Accounting

The Cooperative is a government entity comprised of one enterprise fund which uses the accrual basis of accounting for financial statement purposes. Revenues are recognized in the period in which they become due. Expenses are recognized in the period in which the related liability is incurred.





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2014 AND 2013

NOTE 1 - DESCRIPTION OF THE COOPERATIVE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. Deposits and Investments - Credit Risk, Concentrations of Credit Risk and Interest Rate Risk

Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits - The Cooperative's deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 13-16-15, 13-16-15.1 and 13-16-18.1. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by federal home loan banks accompanied by written evidence of that bank's public debt rating which may not be less than "AA" or a qualified public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

Investments - In general, SDCL 4-5-6 permits Cooperative funds to be invested in (a) securities of the United States and securities guaranteed by the United States government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load mutual fund administered by an investment company whose investments are in securities described in (a) above; and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivision or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

Credit Risk - State law limits eligible investments for the Cooperative, as discussed above. The Cooperative has no investment policy that would further limit its investment choices.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2014 AND 2013

NOTE 1 - DESCRIPTION OF THE COOPERATIVE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. Deposits and Investments - Credit Risk, Concentrations of Credit Risk and Interest Rate Risk (continued)

The Cooperative had the following investments at June 30, 2014 and 2013. All investments are in an internal deposit and investment pool.

	Credit Rating	2014 Market Value	2013 Market Value
Government National Mortgage Assn Real Estate Mortgage Investment Conduits	Not Rated	\$ 12,312	\$ 15,003
Federal National Mortgage Assn Notes	AAA	32,567	33,911
Real Estate Mortgage Investment Conduits	Not Rated	2,554	254,710
Federal Home Loan Mortgage Corp Notes	AAA	281,653	289,073
Real Estate Mortgage Investment Conduits/Collateral Mortgage Obligations	Not Rated	344,805	1,092,207
Federal Farm Credit Bank Notes	AAA	181,895	177,277
Federal Home Loan Bank Notes	AAA	<u>278,013</u>	<u>274,303</u>
Total Investments		<u>\$ 1,133,799</u>	<u>\$ 2,136,484</u>

As of June 30, 2014, the Coop had the following maturities of investments:

	Fair Value	Investment Maturities (in years) Less Than 10	More Than 10
Government National Mortgage Assn Real Estate Mortgage Investment Conduits	\$ 12,312	\$ --	\$ 12,312
Federal National Mortgage Assn Notes	32,567	--	32,567
Real Estate Mortgage Investment Conduits	2,554	--	2,554
Federal Home Loan Mortgage Corp Notes	281,653	--	281,653
Real Estate Mortgage Investment Conduits/Collateral Mortgage Obligations	344,805	--	344,805
Federal Farm Credit Bank Notes	181,895	--	181,895
Federal Home Loan Bank Notes	<u>278,013</u>	<u>--</u>	<u>278,013</u>
	<u>\$ 1,133,799</u>	<u>\$ --</u>	<u>\$ 1,133,799</u>





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2014 AND 2013

NOTE 1 - DESCRIPTION OF THE COOPERATIVE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. Deposits and Investments - Credit Risk, Concentrations of Credit Risk and Interest Rate Risk (concluded)

The Real Estate Mortgage Investment Conduits (REMICs) and Collateralized Mortgage Obligations (CMOs) are categorized based on their due date. Many of the REMICs and CMOs pay principal throughout their life.

The Real Estate Mortgage Investment Conduits (REMICs) and Collateralized Mortgage Obligations (CMOs) above do not qualify as lawful investments under state law.

Interest Rate Risk - The Cooperative does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Concentration of Credit Risk - The Cooperative places no limit on the amount that may be invested in any one issuer.

Custodial Credit Risk - The Cooperative's investments are in a safekeeping account held by RBC Wealth Management which has been designated its fiscal agent. There is no investment policy limiting the amount that can be held by one fiscal agent.

3. Cooperative Benefits

Cooperative liabilities for health claims incurred but not reported are estimated by the third party administrator based on experience and claims filed after the Cooperative's year-end.

4. Cash and Cash Equivalents

For the purpose of the Statement of Cash Flows, the Cooperative considers all highly liquid investments and deposits with a term to maturity of three months or less when purchased to be cash equivalents.





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2014 AND 2013

NOTE 1 - DESCRIPTION OF THE COOPERATIVE AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

5. Estimates

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

6. Revenue and Expense Classifications

In the proprietary fund's Statements of Revenue, Expenses and Changes in Net Position, revenues and expenses are classified in a manner consistent with how they are classified in the Statements of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

7. Equity Classifications

Equity is classified as net position. The Cooperative has only unrestricted net position. Unrestricted net position is defined as all net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

NOTE 2 - UNPAID CLAIMS LIABILITIES

As discussed in Note 1, the Cooperative establishes a liability for both reported and unreported insured events, which includes estimates of future payments and losses. The following represents changes in those aggregate liabilities for the Cooperative during the years ended June 30, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Amounts currently payable and estimated incurred but not reported to or for participants and dependents.		



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2014 AND 2013

NOTE 2 - UNPAID CLAIMS LIABILITIES (CONTINUED)

	<u>2014</u>	<u>2013</u>
Balance at beginning of year	\$ 732,477	\$ 563,604
Claims reported and approved for payment	4,590,453	5,304,622
Claims paid	( 4,590,453)	( 5,304,622)
Increase (decrease) in estimated claims incurred but not reported	( 398,351)	168,873
Balance at end of year	<u>\$ 334,126</u>	<u>\$ 732,477</u>

NOTE 3 - RELATED PARTY

Black Hills Special Services Cooperative (BHSSC) provides office space, office supplies, and wages for the business manager for the Cooperative. The Cooperative reimbursed BHSSC \$300 per month through September 30, 2013 and \$500 a month during the rest of the current year for these expenses for a total of \$5,400 and \$3,600 for the periods ended June 30, 2014 and 2013, respectively.

NOTE 4 - EXCESS RISK HEALTH INSURANCE AND LIFE INSURANCE

The Cooperative purchases excess risk insurance covering claims over \$70,000 per policy year per covered person. The policy has an unlimited annual and lifetime limit. The Cooperative also purchases life insurance for plan participants.

NOTE 5 - ELIGIBLE INVESTMENTS

The Cooperative has invested in Real Estate Mortgage Investment Conduits (REMICs) and Collateralized Mortgage Obligations (CMOs) which, because they are derivatives of the underlying securities, do not qualify as lawful investments under SDCL 4-5-6. These investments make up 17% of total investments.

The Cooperative has ceased investing in REMICs and CMOs and has sold a significant portion of the existing portfolio.



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
NOTES TO FINANCIAL STATEMENTS (CONCLUDED)  
JUNE 30, 2014 AND 2013

NOTE 6 - RISK MANAGEMENT

The Cooperative is exposed to various risks of loss related to torts and errors and omissions. During the period ended June 30, 2014, the Cooperative managed its risks as follows:

Liability Insurance

The Cooperative purchases liability insurance for risks related to torts and errors and omissions of directors and officers from a commercial carrier. There have been no claims resulting from these risks during the past three years.

NOTE 7 - SUBSEQUENT EVENTS

The Cooperative had no subsequent events requiring recording or disclosure in the financial statements through November 12, 2014, which is the date the financial statements were available for issue.





BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
SCHEDULE OF AUDIT FINDINGS  
JUNE 30, 2014

PRIOR AUDIT FINDINGS

Finding 2013-1 Segregation of Duties

This finding has been restated as current audit finding 2014-1.

Finding 2013-2 Qualified Investments

This finding has been restated as current audit finding 2014-2.

CURRENT AUDIT FINDINGS

Finding 2014-1 Segregation of Duties

Criteria

A good system of internal accounting control includes the segregation of duties of accounting personnel, where no one individual has control over the assets, records transactions, and authorizes transactions.

Condition

Black Hills Educational Benefits Cooperative (BHEBC) does not have an adequate segregation of duties over the general operating and investment accounts.

Cause

The size of the BHEBC staff does not provide for an optimum segregation of duties, although several compensating monitoring controls have been implemented.

Effect

One person has control of the assets, records transactions and authorizes transactions.

Recommendation

Many compensating monitoring activities have been implemented using the board of directors and Black Hills Special Services Cooperative employees. The board of directors and manager should continue to implement and perform all practical oversight and review functions.

Management's Response

BHEBC does not employ any staff. BHEBC contracts with Black Hills Special Services Cooperative (BHSSC) for fiscal services. Because of the limited number of banking, investment, and general ledger transactions during the year, the fiscal services are provided



BLACK HILLS EDUCATIONAL BENEFITS COOPERATIVE  
SCHEDULE OF AUDIT FINDINGS (CONTINUED)  
JUNE 30, 2014

CURRENT AUDIT FINDINGS (CONTINUED)

Finding 2014-1 Segregation of Duties (Continued)

primarily by the business manager, with compensating monitoring activities by the board of directors, the independent claims administrator and other BHSSC staff. All premiums received are monitored by the independent claims administrator, Wellmark, and all individual claims paid are reviewed, approved and paid by Wellmark. Due to its size, it is not cost beneficial to take further corrective action.

Finding 2014-2 Qualified Investments

Criteria

The Cooperative is required to follow SDCL 4-5-6 requirements for investments.

Condition

Investments in Real Estate Mortgage Investment Conduits (REMICs) and Collateralized Mortgage Obligations (CMOs) of the Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC) and Government National Mortgage Association (GNMA) do not qualify as lawful investments under SDCL 4-5-6.

Cause

The BHEBC and its fiscal agent, RBC Wealth Management, were unaware that the REMICs and CMOs were not lawful investments under South Dakota law.

Effect

The Cooperative is invested in unlawful investments.

Recommendation

The Cooperative should cease its investment in REMICs and CMOs and take all prudent steps to dispose of existing REMICs and CMOs in its portfolio.

Management's Response

BHEBC has instructed RBC Wealth Management to discontinue investing in these securities. The majority of these investments have been sold. The remaining will be sold as necessary to pay claims.

